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STRICTLY PRIVATE AND CONFIDENTIAL 14 June 2024
The Trustee of the Baptist Pension Scheme
(By e-mail)

Dear Trustee Directors

Baptist Pension Scheme – DC Section (“the Scheme”)
Statutory Money Purchase Illustrations as at 5 April 2024

The Trustee has delegated to Broadstone the responsibility of providing members of the DC Section of the Baptist Pension Scheme with a Statutory Money Purchase Illustration (“SMPI”) each year in respect of their Defined Contribution (“DC”) funds.

The purpose of this letter is to set out the assumptions that the Trustee will need to adopt for the purposes of the SMPIs as at 5 April 2024.

The letter is subject to and complies with the Technical Actuarial Standard TAS 100. The letter has been subject to an independent peer review in accordance with the requirements of the Actuarial Profession Standard APS X2: Review of Actuarial Work.

Background

The legislation and guidance relating to the production of SMPIs are covered by Section 113 of the Pension Schemes Act 1993 and associated regulations, together with the Actuarial Standard Technical Memorandum - AS TM1: “Statutory Money Purchase Illustrations”, as adopted by the Financial Reporting Council on 6 April 1997. I have referred to these collectively as “the SMPI rules”.

In October 2022, a revised version of AS TM1 (version 5.0) was published, effective for SMPIs issued on or after 1 October 2023. In February 2024, AS TM1 version 5.1 was published which comes into effect for illustration dates on or after 6 April 2024. Version 5.0 will be used to determine assumptions for the 5 April 2024 illustrations.

The legislation (and guidance from the Financial Reporting Council) lays down most of the assumptions that should be used, which I summarise in this letter, and compare against those used last year.

It should be noted that the SMPI rules under AS TM1 version 5.0 lead to some material changes to the illustrations that will be produced this year, despite some of the changes being incorporated into last year’s statements to phase in the impact. It should be noted that AS TM1 version 5.1 makes further amendments, which, in the absence of any further changes, means the accumulation rates for volatility groups 1-3 will increase by 1% p.a. next year.

Member options at retirement date

In accordance with the latest rules, SMPIs must be prepared with the assumption that:

- members do not take a tax-free cash lump sum on retirement (i.e. all of their fund is used to provide a pension);
- the pension purchased with their fund will not increase once in payment;
- the pension purchased will be guaranteed for 5 years; and
- the pension purchased by their fund will not include a provision to pay a dependant's pension on the death of the member.

A dependant's pension can be included in the projection if it must be provided under the Scheme Rules. As this is not a requirement under the Scheme Rules, this is not required for the pension illustration.

This basis is the same as used for the Scheme in 2023 and prior years, so there is no change required for 2024.

For active members, projections will be provided assuming contributions will continue at their current rate. There is no requirement to provide illustrations on the alternative basis used last year, which assumed that contributions increased in future by £50 a year. In the interest of consistency and simplicity we propose not to provide the additional illustration this year.

Inflation and future earnings increases

The SMPI Rules prescribe that future prices and earnings must be assumed to increase at 2.5% per annum. The Trustee does not therefore need to consider these assumptions further, and they are the same as used in previous years.

Assumed rate of investment returns (or accumulation rate)

Under the SMPI rules applicable to an illustration date of 5 April 2024 the accumulation rates must be determined according to each investment fund's "volatility group" which is prescribed by the FRC as shown below.

Volatility		Volatility Group	Accumulation Rate
Equal to or above	**Less than**		
0%	5%	1	1% p.a.
5%	10%	2	3% p.a.
10%	15%	3	5% p.a.
15%	Unlimited	4	7% p.a.

Previously, the SMPI rules required that the Trustee took account of the expected returns from the current and anticipated investment strategy of the members' funds over the period to their retirement. Each fund type will now have its own accumulation rate based on the volatility group, these are shown in the table in Appendix A.

The SMPI rules stipulate that the volatility for each fund be calculated from monthly returns of the fund over a five-year period ending on 30 September preceding the financial year in which the calculation is performed. For this purpose, we have interpreted "the financial year in which the calculation is performed" to mean the effective date of the statements – 5 April 2024. The volatility calculations have therefore been completed for the period ending 30 September 2022. It should be noted that we have received volatility data from LGIM that is specific to the funds used by the Scheme, most of which have an inception date of April 2019, so it does not cover the full five-year period. Therefore, as required under the SMPI rules, we have used the volatility data for similar funds to complete the full five-year data set.

Investment Expenses

The SMPI rules require that an allowance should be made for the actual expenses that will be levied on the members' funds before retirement. Where future charges or expenses are not known and cannot reasonably be obtained or estimated, an assumed rate of 1% per annum can be applied. The expenses are set out in the table shown in Appendix A are the actual 'ongoing charges' or 'Total Expense Ratio - TER' as at 31 December 2023, as notified to Broadstone by LGIM. We propose to use the actual charges applicable to each of the funds. This is broadly consistent with the approach adopted in previous years, though certain funds with similar charges were grouped for simplicity.

Annuity rates

The SMPI rules also prescribe that the interest rate underlying annuity rates (which do not increase in payment) must be calculated based on the yield on the FTSE Actuaries Government 15-year Fixed Interest Yield Index rounded to the nearest 0.2%. The yield is determined on 15 February and fixed for the following tax year, so that for an illustration date of 5 April 2024 market yields on 15 February 2023 must be used.

Based on the indices applying on 5 April 2024 (ie. market conditions as at 15 February 2023), this implies **an assumed annuity interest rate 3.8% per annum**, which compares to 1.6% that was used last year.

Please note that the larger increase in assumed annuity interest rates will lead to much higher projected pensions, all other things being equal. However, the impact is likely to be mitigated by the reduced accumulation rates being used under the revised SMPI rules this year.

Mortality rates

The SMPI rules prescribe the mortality assumptions to be used (as set out in Appendix B).

There is a requirement to update the version of the CMI mortality improvements model (to reflect updates to the model based on additional mortality data collected) and we will allow for this when preparing the figures.

The rules have also updated the base tables from PCUA08 tables to PCUA16 tables.

Other assumptions

All other assumptions are prescribed under the SMPI rules and are set out in Appendix B.

Summary

The Trustee will need to adopt the assumptions as required under AS TM1 (version 5.0) as outlined as above and in the Appendices.

The main difference between last year's statement is the increase in the annuity interest rate, which would increase the projected pension by approximate 20-25%.

This will be offset by a reduction in accumulation rates assumed for the equity and diversified growth funds of around 1.5% p.a. – 2.0% p.a. The bond funds however will use a higher assumed accumulation rate than previous year end. This increase could be counterintuitive compared to previous years' experience, but you will be aware of the significant volatility in bond markets more recently which has aligned the funds to a higher volatility group, feeding through to the assumed accumulation rates.

Members invested in the lifestyle funds (the significant majority) further from retirement should expect to see a lower pension projection as the impact of the lower accumulation rates outweighs the increase in the annuity interest rate. Members invested in the lifestyle funds closer to retirement will see a higher pension projection from the impact of the higher accumulation rate on the at-retirement fund and the increase in the annuity interest rate.

While there will be variations between the membership, the changes should not be substantial enough to cause significant concern or warrant any additional communication. But we would be happy to provide some illustrations and test this in more detail if the Trustee is concerned.

If you would like to consider the impact on member projections in more detail and any associated communications, please let me or Richard Sweetman know.

Your sincerely,

C. Rice

Christopher Rice, FIA
Head of Trustee Services

Appendix A – Volatility groups and expenses for each fund

Individual self select funds

Fund name	Volatility group at 5 April 2024	Expenses	Assumed long-term rate of return p.a. at 5 April 2024	Assumed long term rate of return used at 5 April 2023
L&G AAA-AA-A Corporate Bond All Stocks Fund	2	0.12%	3%	1.5%
L&G Over 5 Year Index Linked Gilts Index Fund	4	0.08%	7%	1.5%
L&G All Stocks Index-Linked Gilt Fund	3	0.08%	5%	1.5%
L&G All Stocks Fixed-Interest Gilt Fund	2	0.08%	3%	1.5%
L&G Cash Fund	1	0.10%	1%	1.5%
L&G World Emerging Markets Equity Index	3	0.47%	5%	7%
L&G Global Equity 30:70 Currency Hedged	3	0.23%	5%	7%
L&G Ethical Growth Fund	3	0.173%	5%	7%
L&G Ethical Diversified Fund	2	0.162%	3%	4.5%
L&G At Retirement Fund	2	0.174%	3%	1.5%
L&G Newton Real Return Fund	2	0.84%	3%	4.5%
L&G Dynamic Diversified Fund	2	0.48%	3%	4.5%
L&G Columbia Threadneedle Responsible Global Equity Fund	3	0.75%	5%	7%
L&G Ethical Global Equity Fund	3	0.12%	5%	7%
L&G Low Carbon Transition UK Equity Fund	3	0.058%	5%	7%
L&G Diversified Fund	2	0.29%	3%	4.5%

Impact on lifestyle funds

Ethical default lifestyle

Period from retirement	5 April 2024 (after expenses) p.a.		5 April 2023 (after expenses) p.a.	
	Investment return in that year	Average investment return over period to retirement	Investment return in that year	Average investment return over period to retirement
30	4.83%	4.15%	6.83%	5.68%
25	4.83%	4.02%	6.83%	5.46%
20	4.83%	3.83%	6.83%	5.14%
15	4.83%	3.52%	6.83%	4.61%
10	3.83%	3.11%	5.58%	3.84%
5	2.84%	2.83%	4.33%	2.82%
0	2.83%	2.83%	1.33%	1.33%

Lump sum target lifestyle

All members are within one year of, or over, target retirement age so no projections will be completed.

Appendix B – Statutory assumptions for SMPIs as at 5 April 2024

Assumption	Previous requirement	Revised requirement from 1 October 2023
Projection of Assets (accumulation rate)	Trustee previously had flexibility over the investment returns used to project asset values based on the fund type.	Based on the criteria set out by the FRC asset returns will now be based on which volatility group the fund falls into. (see Accumulation Rate Section)
Increases to Pension in Payment	Choice of whether increasing / non increasing in payment	Non increasing in payment (unless there is a legal requirement)
Annuity Discount Rate in financial year 6 April 20YY to 5 April 20YY+1	Yield date 15 February from the prior financial year **Increasing annuity:** The average of the 5 year Index Linked gilt yield at 0% inflation and 5 year Index Linked yield at 5% inflation, less 0.5% and rounded down to the nearest multiple of 0.2% **Non increasing: (either)** Above increasing rate + 3.5% p.a. **<u>or</u>** FTSE Actuaries' Government 15 year Fixed Interest Yield Index, rounded to the nearest multiple of 0.2%	Yield date 15 February from the prior financial year FTSE Actuaries' Government 15 year Fixed Interest Yield Index, rounded to the nearest multiple of 0.2%
Inflation	2.5% p.a.	2.5% p.a.
Spouse Pension	Choice of whether to include a spouse's pension	No spouse pension (unless there is a legal requirement)
Guarantee period	5 years	5 years
Mortality post 6 April 20YY	PCUA08 (YOB) CMI (20YY-2) 1.25%	PCUA16 (YOB) CMI (20YY-2) 1.25%
Annuity expenses	4%	4%

The SMPI rules (AS TM1 v5.0) require that the following key assumptions must be made:

- Future inflation and earnings increases are assumed to be 2.5% per annum;
- The accumulation rate must be based from the volatility group that the fund falls into;
- Pensions are payable monthly in advance;
- The interest rate underlying annuity rates that do not increase in payment must be calculated as equal to the FTSE Actuaries Government 15 year Fixed Interest Yield rounded to the nearest 0.2%.
- The indices referred to in the paragraphs above are specified as those applying on the 15 February and should be used for all illustrations issued (or with effective dates) in the following financial year;

- A 4% expense loading must be added to the cost of purchasing the annuity;
- Regular charges that are deducted from funds remain at the current level;
- No allowance is to be made for mortality before retirement;
- Mortality after retirement must be based on 50% of the PMA16 tables with allowance for future improvements based on CMI_2021_M[1.25%] plus 50% of the PFA16 tables with allowance for future improvements based on CMI_2021_F[1.25%] ;
- Any spouse's pension has been removed from the annuity, unless there is a legal requirement to provide these.